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Before the  
FEDERAL COMMUNICATIONS COMMISSION  
Washington, DC 20554

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FEDERAL COMMUNICATIONS COMMISSION  
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In the Matter of

Annual Assessment of the Status of  
Competition in the Market for the  
Delivery of Video Programming

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CS Docket No. 95-61

**COMMENTS OF GTE**

GTE Service Corporation and its affiliated  
domestic telephone operating companies

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## SUMMARY

In these Comments, GTE establishes that little has changed with respect to cable operators' entrenched monopoly position since the Commission's *1994 Competition Report*. Indeed, cable operators have been substantially successful in utilizing the regulatory process to forestall telephone company entry into the market for the delivery of video services. To date, commercial video dialtone service has yet to be offered to even a single customer.

If the Commission truly desires to introduce competition in the video marketplace, the Commission must:

- Permit flexibility in the design of channel allocation and sharing plans by LECs that continue to rely on analog channel capacity.
- Increase the "attributable interest" standard in programmers from 5% to 49% equity ownership or control.
- Eliminate or streamline the Section 214 process such that regulatory delays in the offering of VDT services, and the cable industry's ability to game the process, are eradicated.
- Permit a range of options for LECs proposing to offer video programming services, *e.g.*, Title II common carrier or Title VI cable system, as part of integrated or stand alone networks. Do not overlay Title VI rules on Title II services.
- Allow LEC tariff and pricing policies to respond to market conditions rather than rigid rate structure or cost allocation rules. Specifically, the Commission should treat VDT as a non-dominant offering, subject to streamlined tariff regulation.

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**COMMENTS OF GTE**

GTE Service Corporation, on behalf of its affiliated domestic telephone companies, respectfully submits these Comments in response to the Commission's Notice of Inquiry in CS Docket No. 95-61, FCC 95-186, released May 24, 1994 (*Notice*).

**I. INTRODUCTION.**

As the Commission is well-cognizant, deregulation of the cable industry in 1984<sup>1</sup> achieved a number of public policy goals, but was patently unsuccessful in one vital area: creating a competitive multichannel video distribution marketplace.

*Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation*, 8 FCC Rcd 5631, 5638 (¶ 7) (1993), pets. for review denied in relevant part *sub nom. Time Warner Entertainment Co. v. F.C.C.*, 1995 U.S.App.LEXIS 13859 (June 6, 1995), pets. for rehearing pending. To remedy this situation, and the cable industry's consequent abuses of its monopoly position, Congress enacted the 1992 Cable Act,<sup>2</sup> making specific findings that the "cable industry

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<sup>1</sup> Cable Communications Policy Act of 1984, Pub. L. No. 95-549, 98 Stat. 2779 (1984).

<sup>2</sup> Cable Television Consumer Protection and Competition Act of 1992, Pub. L. No. 102-385, 106 Stat. 1460 (1992).

ha[d] become highly concentrated" and that "most cable television subscribers have no opportunity to select between competing cable systems" resulting in "undue market power for the cable operator as compared to that of consumers and video programmers." Pub. L. 102-385, § 2(a)(2), (a)(4); *U S West, Inc. v. United States*, 48 F.3d 1092, 1096 (9th Cir. 1994). Unfortunately, precious little has changed to this day.

In light of the cable industry's virtual stranglehold on the video marketplace, the 1992 Cable Act directed the Commission to submit a report annually to Congress on the status of competition in the market for the delivery of video programming. 47 U.S.C. § 548(g). The Commission issued its first report on September 28, 1994. *Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming, First Report*, CS Docket No. 94-48, 9 FCC Rcd 7442 (1994) (*1994 Competition Report*).

In its *1994 Competition Report*, the Commission specifically found that monopoly wireline cable systems continued to control substantial market power at the local distribution level. *1994 Competition Report*, 9 FCC Rcd at 7449 (¶ 13). While also finding that subscribership had not yet reached a level to conclude that any significant rivalry existed in the market for multichannel video programming distribution, the *1994 Competition Report* did opine that alternative media had made some limited strides since the Commission 1990 Cable Report, specifically in the development of Direct Broadcast Services (DBS), Multipoint Multichannel Distribution Services (MMDS) or "wireless cable", Satellite Antenna Master Television (SMATV) systems and LEC video dialtone (VDT) services. *Id.*, 9 FCC Rcd at 7449-50 (¶ 15). Accordingly, the Commission concluded that the "outlook for improved market performance in

multichannel video distribution markets as a consequence of increasing competitive rivalry remains promising." *Id.*, 9 FCC Rcd at 7556 (¶ 246).

In this proceeding, the Commission undertakes the task of gathering information to assess the status of competition for purposes of submitting its 1995 annual report to Congress and to evaluate changes that have taken place in the competitive environment since the *1994 Competition Report* was issued. The Commission also seeks recommendations for promoting further competition in the market for the delivered video programming. *Notice*, at ¶ 96.

GTE believes that this and future reports should prove to be valuable in crafting changes in regulatory policy as nascent competition ultimately begins to emerge in the video distribution marketplace. However, if competition is indeed to flourish, as postulated by the *1994 Competition Report*, the penchant for overregulation of LECs -- simply because of their status in the telephony market -- must be quickly discarded. While the cable industry has been substantially successful in derailing the competitive threat posed by LECs in the nearly three years since the Commission first adopted its video dialtone (VDT) policy,<sup>3</sup> the Commission now has the opportunity in this and related dockets to refocus its video policies so that consumers will be able to achieve true competitive benefits from alternative video providers in a timely and efficient manner. To do this, LECs must be recognized for what they are: fledgling entrants

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<sup>3</sup> *Telephone Company - Cable Television Cross-Ownership Rules, Section 63.54-63.58*, Second Report and Order, Recommendation to Congress, and Second Further Notice of Proposed Rulemaking, 7 FCC Rcd 5781 (1992) (*Video Dialtone Order*), pets. for review pending *sub nom. Mankato Citizens Telephone Co. v. F.C.C.*, No. 92-1404 (D.C. Cir.).

constrained by regulation at every turn into a marketplace dominated by well-financed, entrenched and aggressive monopolists.

In these Comments, GTE responds to questions posed in the *Notice* regarding LEC VDT networks and recommends specific regulatory policy changes which, if adopted, will serve to advance the opportunity for competition in the delivery of video programming services.

## **II. DEFINING THE MARKET FOR DELIVERED VIDEO PROGRAMMING - VIDEO DIALTONE SERVICES.**

The *1994 Competition Report* speculated that LEC VDT networks would in the future provide competition to entrenched cable operators. However, since issuance of the *1994 Competition Report*, virtually nothing has changed to alter cable operators' overriding monopoly positions. LECs have not been able to offer VDT service on a commercial basis, despite the time which has elapsed since the Commission's *Video Dialtone Order*. Indeed, the Commission's regulatory framework for VDT remains fluid, thereby injecting great uncertainty into the marketplace. In light of both technological changes and the Commission's regulatory environment, potential VDT providers -- including GTE -- are currently re-examining their video plans. Some are already eschewing the VDT model.<sup>4</sup> Others have adopted a wait-and-see approach. Depending upon the Commission's anticipated action in the generic video dialtone

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<sup>4</sup> See *Communications Daily*, v. 15, no. 124, June 28, 1995 ("Ameritech abandoned VDT approach and will follow cable model ... Chairman-CEO Richard Notebaert said Tuesday.").

docket,<sup>5</sup> VDT could be either a viable market competitor to cable or a stillborn regulatory fantasy.

The *Notice* requests comments on the following aspects of potential LEC VDT service deployment:

- (a) How will the prices and services offered over VDT networks compare to the prices and services charged by cable operators? How will this comparison change over time? What is the basis for this prediction?

GTE's analysis of its first four VDT markets indicates that, initially, subscribers will be willing to pay monthly charges of approximately \$35 for a combination of basic, expanded, premium and enhanced video services. This is consistent with comparable charges assessed by local cable operators in these markets. However, GTE expects per subscriber revenues to rise to as much as \$70 per month within a ten year period. The capabilities and capacities of GTE's networks are expected to expand the range of service options available to end users to levels that well exceed those of current closed cable systems.

Notwithstanding this analysis, the prices and services offered by programmers using VDT systems will only be competitive with existing cable offerings if LECs are afforded the flexibility to accommodate the unique needs of a varied set of programmers. Prices of programming packages and services will be directly impacted by the level of transport charges that LECs assess pursuant to their VDT tariffs.

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<sup>5</sup> *In re Telephone Company - Cable Television Cross-Ownership Rules, Sections 63.54 - 63.58, CC Docket No. 87-266, Third Further Notice of Proposed Rulemaking, FCC 94-269, released November 7, 1994, and Fourth Further Notice of Proposed Rulemaking, FCC 95-20, released January 20, 1995 (Third and Fourth Further Notices).*



Therefore, in order to be successful, LECs must be able to design pricing structures which support both the needs of larger multichannel service packagers as well as smaller *a la carte* programmers. In addition, LECs must be allowed to modify rate levels and structures as changing market conditions dictate.

GTE believes that in a market where VDT programmers seek to compete against established cable companies which continue to control substantial market share, the Commission should properly treat VDT as a non-dominant service subject only to "streamlined" regulation.<sup>6</sup> Only by allowing market forces to govern VDT rates will programmers utilizing VDT networks be positioned to offer rates and service packages to subscribers that are competitive with existing cable offerings, thereby bringing the benefits of competition to consumers.

Similarly, VDT programmer-customers will be able to package truly competitive video programming offers to subscribers only if they are able to obtain sufficient capacity on LEC VDT networks. Thus, GTE has repeatedly urged the Commission to permit LECs the flexibility to design operational plans that accommodate evolving capacity needs as new technologies become increasingly economical and their deployment more efficient.<sup>7</sup> And yet the Commission has imposed, and is considering additional, restrictions which could prohibit LECs from furnishing *sufficient* analog capacity to new entrants seeking to compete in local video programming markets

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<sup>6</sup> See 47 C.F.R. Section 61.22. See also *Treatment of Video Dialtone Services Under Price Cap Regulation*, CC Docket No. 94-1, Further Notice of Proposed Rulemaking, FCC 95-49, GTE Comments, dated April 17, 1995.

<sup>7</sup> See *Third Further Notice*, GTE Comments, December 16, 1995, at 3; *In re Contel of Virginia, Inc., et al.*, W-P-C-6955, GTE Reply Comments and Consolidated Opposition to Petitions to Deny, February 2, 1995, at 30.

against incumbent cable providers. GTE believes that the Commission must refrain from creating such restrictive channel allocation requirements and allow LECs to implement channel sharing proposals that reflect the needs of individual local distribution markets.<sup>8</sup>

- (b) What are the technological impediments and advantages to the deployment of VDT platforms as competitive alternatives to cable systems?

Initially, GTE plans to construct hybrid fiber-coaxial systems which will provide 80 analog and 168 compressed digital channels. GTE's use of digital compression technology will enable it to significantly expand capacity on its networks as demand for from programmers increases. Digital compression represents a new method of delivering a greater number of programming services to subscribers as opposed to traditional analog cable television networks. Digital transmission promises to enhance a programmer's ability to provide interactive, informational and pay-per-view services.

In the short term, VDT platforms must continue to rely on analog delivery mechanisms due to the limited availability of digital technology and the cost of placing digital set-top box equipment on every subscriber television set in the VDT delivery area. However, consistent with the Commission's directive,<sup>9</sup> digital technology will be available on day one of GTE's VDT service deployment. End-users who are interested

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<sup>8</sup> For example, in GTE's proposed Thousand Oaks, CA VDT serving area, the existing cable television system has an analog channel capacity 54 channels; in St. Petersburg, FL, 78 channels; in Honolulu, HI, 36 channels. The variances in these cable service offerings demonstrate the need for LECs to create voluntary channel allocation and sharing plans which will maximize the amount of analog capacity available to programmers in their individual serving areas.

<sup>9</sup> *In re Contel of Virginia Inc.*, DA 95-1012, released May 5, 1995, at ¶ 117.h.

in subscribing only to offerings transmitted on analog channels will have the option of utilizing a lower-cost, lower-functionality decoder, capable of descrambling analog signals only. End-users who desire to subscribe to both these programmer offerings and those which are transmitted on digital channels will require a higher-end, hybrid analog/digital decoder.

GTE anticipates that customer-programmers will make both analog and digital services available initially and that switched digital interactive services will be introduced during 1996. Based upon vendor commitments, GTE anticipates the delivery of sufficient hybrid analog/digital decoders as well as digital compression equipment by the end of 1995. Analog decoders are available from a variety of manufacturers today. GTE fully expects that over time, the costs of providing digital set top and network functionalities will diminish, permitting VDT providers to expand capabilities to programmers that wish to offer advanced interactive, video-on-demand, and enhanced services to subscribers.

- (c) What is the status of the build-out of systems for which Section 214 authorizations have been granted?

GTE was granted Section 214 Authorization by the Common Carrier Bureau to begin construction and operation of VDT networks in four serving areas.<sup>10</sup> GTE tentatively plans to begin construction this summer in at least two of these markets. Construction plans for other systems have yet to be finalized. GTE anticipates that VDT services will be made available to programmer-customers and GTE local

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<sup>10</sup> See n. 10.

subscribers in the first quarter of 1996. However, the achievement of this implementation date will depend on a number of factors, specifically including the outcome of regulatory proceedings which will impact the ability of GTE to offer competitively viable VDT services on a timely basis.<sup>11</sup>

- (d) Have the plans for deployment of VDT networks for which Section 214 authorizations have been granted, or the plans for deployment of VDT networks that are the subject of applications currently pending before the Commission, been affected by events since the *1994 Competition Report*?

The rate of deployment of VDT services has been primarily impacted by two factors: (1) technological developments (especially in digital technology), and (2) evolving regulatory policies. Specifically, changing expectations of digital software and hardware development have affected deployment plans of not only GTE but other LECs as well.<sup>12</sup> The telephone industry has had sufficient expertise in managing changing technological advancements during the past decade and now considers such changes "normal" aspects of doing business. However, GTE is concerned that the Commission is diverging from its earlier commitment to adopt a flexible regulatory approach and is

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<sup>11</sup> In addition to the Commission's anticipated actions on the *Third and Fourth Further Notices*, of particular importance is timely approval of GTE's Part 69 waiver to establish a VDT rate structure and GTE's channel reservation and general VDT tariffs. In order to properly streamline the process, GTE has urged the Commission to eliminate the requirement that LECs first obtain a waiver of Part 69 prior to tariffing VDT services. GTE Comments in response to Ameritech's Petition for Reconsideration, February 9, 1995, at 5-7. The Part 69 requirement simply delays the delivery of competitive video services to local subscribers because adequate review of LEC rate structures, as well as underlying costs, can be performed within the tariff review process.

<sup>12</sup> For example, GTE was required to amend its Section 214 Applications to reflect the availability of digital set-top equipment. See *In re Contel of Virginia, Inc., et al.*, Amendments, December 16, 1995, at 2. Other LECs, such as Bell Atlantic and U S West, have postponed their commercial VDT offerings in order to evaluate technological alternatives. Like Bell Atlantic and U S West, GTE continues to evaluate changing technological conditions and how they might impact broadband network deployment.

layering VDT with unnecessary regulation. Indeed, if each technology change requires amendment of a LEC's VDT authorization, then these networks may never be built. LECs must have flexibility to adapt to technological changes in a timely fashion without the delay inherent in the Section 214 process which continues to be subverted by the cable industry.

Additionally, as the Commission recognizes in the *Notice* (at ¶¶ 48-50), several significant court decisions have been rendered since the *1994 Competition Report* which directly affect LEC VDT plans. And the Commission itself has several ongoing proceedings in which it is considering a number of issues vital to VDT deployment. These proceedings will significantly impact VDT offerings, either making VDT a viable competitor to entrenched cable systems or relegating the VDT to the competitive dustbin.

In light of several court decisions which have overturned the statutory ban on LEC provision of programming, 47 U.S.C. § 533(b), LECs may now offer programming services directly to subscribers over its VDT platforms or via a cable system subject to Title VI regulation. In the *Fourth Further Notice*, the Commission is considering the application of additional regulations to LECs, or their affiliates, that plan to provide programming services to end users. Among these proposals are those which would apply the full range of Title VI restrictions on LEC programming operations *in addition to* the extensive set of Title II regulations to which LECs are currently subject. If adopted,

this approach will have the effect of encouraging LECs to abandon the VDT model and operate closed cable systems subject to Title VI.<sup>13</sup>

In the *Third Further Notice* and its LEC price cap review proceeding, the Commission is considering the establishment of rules and policies regarding the allocation and sharing of channels on VDT networks, preferential access, and the application of price cap regulation to VDT. GTE readily expects that the outcome of these proceedings will impact video business plans. For example, if allocation and sharing policies restrict the ability of VDT programmers to construct service packages that may viably compete with existing cable offerings, demand for GTE's VDT service would become non-existent and result in stranded investment and waste of resources. In addition, application of additional pricing restrictions on GTE after it has established its initial VDT prices (such as the imposition of pricing bands and subelements under price caps) would severely limit GTE's ability to compete against incumbent cable firms, which may not be rate regulated themselves.<sup>14</sup> These are further examples of why it is vital for the Commission to adopt flexible regulatory policies that allow VDT to evolve as technology, and markets, change.

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<sup>13</sup> The Commission has also issued an *Enforcement Policy* which purportedly requires LECs pursuing the Title VI cable option to first obtain Section 214 authority. Despite the Commission's earlier pronouncements to Congress that provision of LEC programming services would enhance the availability of video services to the American public, the *Enforcement Policy* represents yet another regulatory roadblock to full and fair competition in the video markets. Indeed, the *Enforcement Policy*, which is nothing more than a "back door" attempt to resurrect the video programming ban, that is itself both unconstitutional and exceeds the Commission's statutory authority. See *United States Telephone Association v. F.C.C.*, No. 95-533-A (E.D.Va., Amended Complaint filed June 22, 1995).

<sup>14</sup> For example, once alternative video distribution services are present in a cable operator's market, it no longer is subject to any rate regulation, either from the local franchise authority or the Commission. Just as important, LECs should be afforded the pricing flexibility to meet competition to their VDT offerings.

The *Notice* (at ¶ 55) also seeks comment on the competitive implications of recent joint venture developments involving VDT providers. Joint programming development ventures should not be viewed as "evils" since they will result in new and diversified sources of programming, which the Commission is statutorily directed to encourage.

- (e) What are the current plans for deployment of VDT systems that are not currently the subject of applications before the Commission?

GTE's plans call for the development of competitive video networks within a total of sixty-six markets throughout the nation, effectively providing competitive video services to nearly 7 million homes within the next nine to ten years. While GTE currently has no definitive plans to submit additional Section 214 applications for VDT, it is evaluating additional markets to determine the competitive viability of constructing alternative video distribution networks. Based on a number of economic, market, and regulatory factors, GTE may elect to build Title VI cable systems in some of its serving territories and VDT networks in others.

- (f) Are there particular market characteristics, such as high population density, that are necessary to support competition between VDT and cable systems? Will this limit competition to certain types of geographic areas, such as large metropolitan areas?

The development of GTE's video deployment plans is based on sensible market selection criteria to determine initial service roll-out markets. GTE chose its initial markets from all of its telephone serving areas based on a mix of different geographic and competitive profiles, including population density and the status of competition. GTE analyzed and grouped contiguous exchange service areas into "market clusters"

within major metropolitan markets based on a "community of interest" standard. The chosen markets reflected population densities and existing competitive characteristics that indicated levels of consumer demand for video services that would warrant the introduction of a new competitor in the market.

Although wireline VDT services are being introduced initially in major metropolitan areas, alternative distribution media, such as MMDS and SMATV, are becoming increasingly available in small towns and rural areas. Most LECs are planning to construct wireline video networks; however, the provision of wireless systems may prove to be economically feasible in certain LEC serving areas. The introduction of alternative video sources in rural areas, whether by an existing telephone or non-telephone company, should not be hampered by Commission regulation.

### **III. RECOMMENDATIONS FOR PROMOTING COMPETITION IN THE MARKET FOR DELIVERY OF VIDEO PROGRAMMING.**

The *Notice* requests that parties recommend rules or policies that should be adopted by the Commission to promote additional competition in the market for video programming delivery. GTE contends that imprudent regulation presents the greatest single danger to the future of VDT and LECs' ability to emerge as viable competitors in video markets. LECs entering local video distribution markets, either as a Title II common carriers or Title VI cable operators, will compete with entrenched monopoly cable systems which, by the Commission's own findings, continue to exert monopoly market control over prices and service offerings made available to local subscribers. Therefore, the Commission must first determine whether any proposed rule or policy



impedes a LEC's ability to fashion a viable competitive alternative, on both a price and service basis, to services offered by entrenched cable systems.

If the Commission is to reach its policy goals with respect to the development of VDT, *i.e.*, infrastructure development, programming diversity, increased competition, and enhanced consumer choice, it should adopt the following policy positions:

- Permit flexibility in the design of channel allocation and sharing plans by LECs that continue to rely on analog channel capacity.
- Increase the "attributable interest" standard in programmers from 5% to 49% equity ownership or control.
- Eliminate or streamline the Section 214 process such that regulatory delays in the offering of VDT services, and the cable industry's ability to game the process, are eradicated.
- Permit a range of options for LECs proposing to offer video programming services, *e.g.*, Title II common carrier or Title VI cable system, as part of integrated or stand alone networks. Do not overlay Title VI rules on Title II services.
- Allow LEC tariff and pricing policies to respond to market conditions rather than rigid rate structure or cost allocation rules. Specifically, the Commission should treat VDT as a non-dominant offering, subject to streamlined tariff regulation.

Adoption of these sensible policy directives will provide incentives for LECs to construct and operate open common carrier networks in those markets where VDT services make economic sense. Likewise, LECs will take advantage of Title VI options in those markets in which the operation of a competitive cable system is competitively appropriate. In both instances the winner is the consumer -- a diverse array of video programming alternatives at prices which are dictated by true competition.

#### **IV. CONCLUSION**

GTE urges the Commission to adopt, as a component of its 1995 annual report to Congress, a commitment to craft changes in regulatory policy which reflect the increasing competitive environment in the video distribution markets. Flexible


regulatory policies should be adopted which encourage LECs to become successful in either a Title II or Title VI video endeavor.

Respectfully submitted,

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